

***San Francisco Ballet  
Association***

*Consolidated Financial Statements  
for the Year Ended June 30, 2006, and  
Independent Auditors' Report*

## INDEPENDENT AUDITORS' REPORT

To the Board of Trustees of  
San Francisco Ballet Association  
San Francisco, California

We have audited the accompanying consolidated statement of financial position of the San Francisco Ballet Association (the "Ballet") as of June 30, 2006, and the related consolidated statements of activities and changes in net assets and of cash flows for the year then ended. These consolidated financial statements are the responsibility of the Ballet's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit. The prior year summarized comparative information has been derived from the Ballet's 2005 consolidated financial statements and, in our report dated November 29, 2005, we expressed an unqualified opinion on those financial statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Ballet's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the Ballet as of June 30, 2006, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

*Deloitte + Touche LLP*

November 15, 2006

# SAN FRANCISCO BALLET ASSOCIATION

## CONSOLIDATED STATEMENT OF FINANCIAL POSITION

JUNE 30, 2006

(With summarized financial information as of June 30, 2005)

	2006	2005
<b>ASSETS</b>		
CASH AND CASH EQUIVALENTS	\$ 6,739,764	\$ 5,466,884
ACCOUNTS RECEIVABLE	309,314	323,981
PREPAID EXPENSES AND DEPOSITS	1,288,181	3,535,646
PLEDGES RECEIVABLE—Net	7,144,903	7,424,512
RECEIVABLES FROM SPLIT INTEREST AGREEMENTS—Net	4,695,217	4,667,116
RESTRICTED CASH	562,928	1,092,988
BOND ISSUANCE COSTS—Net	382,440	397,149
PROPERTY AND EQUIPMENT—Net	23,093,943	24,580,369
ENDOWMENT INVESTMENTS	<u>69,726,295</u>	<u>63,335,100</u>
TOTAL	<u>\$ 113,942,985</u>	<u>\$ 110,823,745</u>
<b>LIABILITIES AND NET ASSETS</b>		
LIABILITIES:		
Accounts payable and accrued expenses	\$ 3,142,681	\$ 2,483,424
Line of credit	1,368,158	
Deferred performance and school revenue	2,940,201	4,959,183
Interest rate swap liability	52,000	754,862
Bonds payable	<u>19,540,000</u>	<u>19,540,000</u>
Total liabilities	<u>27,043,040</u>	<u>27,737,469</u>
NET ASSETS:		
Unrestricted	33,063,556	30,273,470
Temporarily restricted	13,994,347	14,463,043
Permanently restricted	<u>39,842,042</u>	<u>38,349,763</u>
Total net assets	<u>86,899,945</u>	<u>83,086,276</u>
TOTAL	<u>\$ 113,942,985</u>	<u>\$ 110,823,745</u>

See notes to consolidated financial statements.

# SAN FRANCISCO BALLET ASSOCIATION

## CONSOLIDATED STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS

YEAR ENDED JUNE 30, 2006

(With summarized financial information for the year ended June 30, 2005)

	2006			Total	2005 Total
	Unrestricted	Temporarily Restricted	Permanently Restricted		
<b>OPERATING REVENUES:</b>					
San Francisco performance	\$ 14,170,570	\$ -	\$ -	\$ 14,170,570	\$ 12,674,963
Touring	402,500			402,500	442,497
School and student housing	1,443,593			1,443,593	1,376,812
Postage and handling fees	425,353			425,353	357,975
Sales and rentals—net	222,329			222,329	157,087
Endowment transfers	4,309,651			4,309,651	4,362,352
Dividend and interest income	71,779			71,779	66,330
Other income	240,458			240,458	105,986
<b>Total operating revenues</b>	<b>21,286,233</b>			<b>21,286,233</b>	<b>19,544,002</b>
<b>OPERATING EXPENSES:</b>					
Program services:					
Ballet production	21,978,076			21,978,076	19,973,454
Touring	830,966			830,966	1,210,987
School and student housing	2,855,555			2,855,555	2,910,877
Education and outreach	461,160			461,160	413,753
<b>Total program services</b>	<b>26,125,757</b>			<b>26,125,757</b>	<b>24,509,071</b>
Support services:					
Marketing, publicity, and audience development	3,518,921			3,518,921	3,226,785
General and administrative	3,788,091			3,788,091	3,135,396
Fundraising	1,649,417			1,649,417	1,647,210
<b>Total support services</b>	<b>8,956,429</b>			<b>8,956,429</b>	<b>8,009,391</b>
Net realized and unrealized (gains) losses on interest rate swap	(630,153)			(630,153)	695,413
<b>Total operating expenses</b>	<b>34,452,033</b>			<b>34,452,033</b>	<b>33,213,875</b>
<b>Operating revenues less operating expenses</b>	<b>(13,165,800)</b>			<b>(13,165,800)</b>	<b>(13,669,873)</b>
<b>CONTRIBUTIONS IN SUPPORT OF OPERATIONS:</b>					
Contributions	8,133,655	3,366,022		11,499,677	12,123,858
Special events and Auxiliary activities—net	1,745,741			1,745,741	1,617,948
Net assets released from restrictions	3,537,769	(3,537,769)			
<b>Total contributions in support of operations</b>	<b>13,417,165</b>	<b>(171,747)</b>		<b>13,245,418</b>	<b>13,741,806</b>
<b>CHANGE IN NET ASSETS FROM OPERATIONS</b>	<b>251,365</b>	<b>(171,747)</b>		<b>79,618</b>	<b>71,933</b>
<b>ENDOWMENT:</b>					
Contributions	534,475	127,609	877,023	1,539,107	4,942,344
Endowment management and expenses	(498,827)			(498,827)	(586,057)
Investment return after transfers to operations	1,386,887	608,840	665,325	2,661,052	1,933,780
Bad debt expense			(50,069)	(50,069)	(25,000)
Net assets released from restrictions	1,033,398	(1,033,398)			
<b>Change in net assets from endowment</b>	<b>2,455,933</b>	<b>(296,949)</b>	<b>1,492,279</b>	<b>3,651,263</b>	<b>6,265,067</b>
<b>BUILDING MAINTENANCE FUND—Dividend and interest income</b>	<b>82,788</b>			<b>82,788</b>	<b>24,563</b>
<b>INCREASE (DECREASE) IN NET ASSETS</b>	<b>2,790,086</b>	<b>(468,696)</b>	<b>1,492,279</b>	<b>3,813,669</b>	<b>6,361,563</b>
<b>NET ASSETS—Beginning of year</b>	<b>30,273,470</b>	<b>14,463,043</b>	<b>38,349,763</b>	<b>83,086,276</b>	<b>76,724,713</b>
<b>NET ASSETS—End of year</b>	<b>\$ 33,063,556</b>	<b>\$ 13,994,347</b>	<b>\$ 39,842,042</b>	<b>\$ 86,899,945</b>	<b>\$ 83,086,276</b>

See notes to consolidated financial statements.

# SAN FRANCISCO BALLET ASSOCIATION

## CONSOLIDATED STATEMENT OF CASH FLOWS

YEAR ENDED JUNE 30, 2006

(With summarized financial information for the year ended June 30, 2005)

	2006	2005
CASH FROM OPERATING ACTIVITIES:		
Increase in net assets	\$ 3,813,669	\$ 6,361,563
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Permanently restricted contributions received	(488,000)	(1,880,300)
Depreciation and amortization	1,882,543	1,303,081
Net realized and unrealized gains on investments	(4,495,801)	(3,780,911)
Limited partnership gain	(1,193,120)	(962,197)
Change in discount and allowance related to pledges receivable	135,531	138,064
Change in fair value of derivative	(702,862)	520,232
Investment income from restricted cash	(27,395)	(65,549)
Net effect of changes in:		
Accounts receivable	14,667	428,428
Prepaid expenses and deposits	2,247,465	(1,743,992)
Pledges receivable	144,078	1,170,868
Receivables from split interest agreements	(28,101)	(383,961)
Accounts payable and accrued expenses	659,257	15,359
Deferred performance and school revenue	(2,018,982)	420,986
Net cash (used in) provided by operating activities	<u>(57,051)</u>	<u>1,541,671</u>
CASH FROM INVESTING ACTIVITIES:		
Purchases of endowment investments	(21,314,654)	(10,756,934)
Proceeds from sales and maturities of endowment investments	20,612,380	8,746,239
Decrease in restricted cash	557,455	4,207,017
Acquisitions of property and equipment	(381,408)	(4,068,852)
Net cash used in investing activities	<u>(526,227)</u>	<u>(1,872,530)</u>
CASH FROM FINANCING ACTIVITIES:		
Permanently restricted contributions received	488,000	1,880,300
Borrowings on line of credit	1,368,158	
Net cash used in investing activities	<u>1,856,158</u>	<u>1,880,300</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	1,272,880	1,549,441
CASH AND CASH EQUIVALENTS—Beginning of year	<u>5,466,884</u>	<u>3,917,443</u>
CASH AND CASH EQUIVALENTS—End of year	<u>\$ 6,739,764</u>	<u>\$ 5,466,884</u>
SUPPLEMENTAL DISCLOSURES—Cash paid during the year for interest	<u>\$ 630,214</u>	<u>\$ 287,040</u>

See notes to consolidated financial statements.

# SAN FRANCISCO BALLET ASSOCIATION

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS YEAR ENDED JUNE 30, 2006

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### 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Organization**—San Francisco Ballet Association (the “Ballet”) operates both a dance company and a ballet school. As America’s first professional ballet company, the Ballet has enjoyed a long and rich tradition of artistic “firsts” since its founding in 1933, performing the first American productions of *Swan Lake* and *Nutcracker*, as well as the first twentieth-century American *Coppélia*. The Ballet is one of the three largest ballet companies in the United States of America with its current roster of seventy-two dancers. The Ballet presents regular performances in San Francisco, California, and other communities in the Bay Area, as well as annual tours to domestic and foreign locations. The San Francisco Ballet Endowment Foundation (the “Foundation”), a separate not-for-profit corporation, holds the assets of the San Francisco Ballet endowment for the benefit of the Ballet.

**Principles of Consolidation**—The accompanying consolidated financial statements include the financial position, changes in net assets, and cash flows of the Ballet and the Foundation because the Ballet has both control of and economic interest in the Foundation. Interorganizational transactions and accounts have been eliminated in consolidation.

**Basis of Presentation**—The accompanying consolidated financial statements are presented on the basis of unrestricted, temporarily restricted, and permanently restricted net assets.

**Cash and Cash Equivalents**—Cash and cash equivalents consist of demand deposits and highly liquid investments purchased with an original maturity of three months or less.

**Pledges Receivable**—Pledges receivable consist of unconditional promises to give that are expected to be collected in future years. Such receivables are recorded at the present value of their estimated future cash flows. The discounts on these amounts are computed using risk-free rates applicable in the years in which those promises were received. Amortization of the discounts is included in contributions in the accompanying consolidated statement of activities and changes in net assets.

**Receivables From Split Interest Agreements**—Receivables from split interest agreements represent the Ballet’s irrevocable remainder interests in a pooled income fund and various trusts held by third-party trustees. These receivables are stated at estimated fair value, which is measured as the present value of the estimated future distributions expected to be received over the expected terms of the agreements. In determining the fair value, the Ballet considers single or joint life expectancy from the 1983 Group Mortality Table, the estimated return on the invested assets during the expected term of the agreements, the contractual payment obligations under the agreements, and a discount rate reflective of current market conditions. The estimation of the fair value of these receivables is subjective and requires significant judgment. Due to uncertainties inherent in the estimation process, it is possible that future events in either the near or long term could materially affect the amounts reported in the consolidated statement of financial position.

**Bond Issuance Costs**—Bond issuance costs are being amortized over the term of the bonds payable. Accumulated amortization as of June 30, 2006 was \$58,837.

**Restricted Cash**—Restricted cash is invested in two guaranteed investment contracts that are held by a trustee in restricted accounts established with proceeds received from the bonds payable.

**Property and Equipment**—Property and equipment are stated at cost. Donated property and equipment is recorded at estimated fair value at the date of receipt. The building and improvements are being depreciated on a straight-line basis over twenty to forty years. Depreciation of furniture and equipment is computed on the straight-line basis over the estimated useful life of the assets, generally three to ten years.

Fixed assets that are donated or acquired with resources restricted for such acquisition are considered to be temporarily restricted and are released from restrictions over the estimated useful life of the asset.

Maintenance expenses and all costs for new productions, including sets, costumes, and choreography, are charged to expense as incurred or in the year of initial performance with the exception of costs associated with full-length works. Full-length works are capitalized and depreciated on a straight-line basis over the first two years the new works are presented. The Ballet's new production of *Nutcracker*, including the costs for sets, costumes, staging, and choreography, completed in 2005, is being depreciated on a straight-line basis over fifteen years.

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

**Endowment Investments**—Endowment investments consist of equity and fixed income investments, limited partnership investments, and cash and cash equivalent balances restricted by donors or designated by the Ballet's Board of Trustees for long-term investment. Investments in equity and debt securities are stated at estimated fair value based on quoted market prices. Other investments, such as limited partnership interests, are also recorded at estimated fair value. Limited partnership interests include nonmarketable and/or restricted investment securities whose values have been estimated by management in the absence of readily determinable fair values. Management's estimates are based on information provided by the managing partner of the limited partnership. Because of the inherent uncertainty of valuation of nonmarketable and restricted investments, those estimated fair values may differ significantly from the values that would have been used had a ready market for the securities existed, and the differences could be material.

Gains or losses that result from market fluctuations are recognized in the period such fluctuations occur. Realized gains or losses resulting from sales of securities are calculated on an adjusted cost basis. Adjusted cost for this purpose is the estimated fair value of the security at the beginning of the year or the cost if purchased during the year. Dividend and interest income is recognized when earned.

**Deferred Performance and School Revenue**—Deferred performance and school revenue at June 30, 2006 primarily consists of advance ticket sales for performances scheduled in the Ballet's 2007 repertory season, which opens in January 2007, as well as advance tuition payments for school classes to be conducted in the year ending June 30, 2007.

**Derivative Instrument**—The Ballet has an interest rate swap agreement ("Swap Agreement"), which is considered a derivative instrument, to manage the interest rate exposure of its bonds by minimizing its exposure to volatility in the market. The Swap Agreement is reflected on the consolidated statement of financial position at estimated fair value.

***Unrestricted Net Assets***—Unrestricted net assets are available to support all activities of the Ballet. Unrestricted net assets include amounts designated by the Ballet’s Board of Trustees for the Building Maintenance Fund (the “Fund”), which totaled approximately \$3,096,000 at June 30, 2006. The Fund was established by the Board of Trustees to provide for the maintenance of the Ballet’s facilities when other financial resources are not available for such purposes. The Ballet’s Board of Trustees determines on an annual basis how much will be designated to or transferred from the Fund with consideration given to the Ballet’s unrestricted operating results and facilities maintenance costs.

***Temporarily Restricted Net Assets***—Temporarily restricted net assets represent contributions whose use is limited by donor-imposed stipulations that expire by the passage of time or can be fulfilled and removed by actions of the Ballet pursuant to those stipulations.

***Permanently Restricted Net Assets***—Permanently restricted net assets represent contributions whose use is limited by donor-imposed stipulations that require the gift to be invested in perpetuity. The income from such invested assets, including realized and unrealized gains, is generally available to support the activities of the Ballet.

***Sales and Rentals***—Sales and rentals are presented net of costs of \$507,236 for the year ended June 30, 2006.

***Revenue Recognition***—All contributions are recognized as revenue when received or unconditionally promised to the Ballet. The Ballet classifies gifts of cash and other assets as temporarily or permanently restricted support if received with donor stipulations that limit the use of the contributions. When such restrictions expire, that is, when a stipulated time restriction ends or a purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported as net assets released from restrictions. Temporarily restricted contributions are reported as unrestricted support when the restriction is met in the same period as the contribution is received. Conditional promises to give are not recognized as revenue until the conditions are substantially met. There were no conditional promises at June 30, 2006.

Investments received as gifts are initially recorded at estimated fair value at the date of donation. The Ballet’s irrevocable interest in split interest agreements is recognized as revenue at the time such agreements are made known to the Ballet.

***Contributions of Services***—Contributions of services are recognized when received if such services (a) create or enhance nonfinancial assets or (b) require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not donated. During the year ended June 30, 2006, the value of contributed services recognized as revenues in the accompanying consolidated financial statements was approximately \$25,000 and consisted primarily of air travel services. In addition, a substantial number of volunteers have donated significant amounts of time in the Ballet’s program services and fund-raising activities through participation in the Auxiliary, Encore!, and Bravo organizations. The value of donated volunteer services has not been recognized in the accompanying consolidated financial statements because such volunteer services do not meet the criteria described above.

***Special Events and Auxiliary Activities***—Special events and auxiliary activities are presented net of costs of \$1,188,668 for the year ended June 30, 2006, including donated food and beverages of approximately \$217,000.

**Functional Expense Allocations**—Expenses, such as depreciation, supplies, travel, personnel, and occupancy costs, are allocated among program services and support services on the basis of occupancy ratios and on estimates made by the Ballet’s management.

**Collective Bargaining Agreements**—Approximately 85% (1,152 employees) of the Ballet’s employees are covered by collective bargaining agreements. Of these employees, 83 are covered under an agreement that expired on June 30, 2006. The renewal of this agreement has been agreed to in principal and is expected to be finalized during 2007.

**Income Tax Status**—The Ballet has been classified as a publicly supported, tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code, and is exempt from California franchise taxes under Revenue and Taxation Code Section 23701(d).

**Fair Value of Financial Instruments**—The Ballet’s financial instruments include cash, cash equivalents, guaranteed investment contracts, accounts receivable, pledges receivable, receivables from split interest agreements, endowment investments, accounts payable and accrued expenses, a Swap Agreement, and bonds payable. For cash, cash equivalents, accounts receivable, and accounts payable and accrued expenses, the carrying amounts approximate fair value because of the short maturity of these items. Endowment investments, guaranteed investment contracts, pledges receivable, receivables from split interest agreements, and the Swap Agreement are reflected at their estimated fair values using methodologies described above. The carrying amount of the bonds payable represents a reasonable estimate of the corresponding fair value due to the associated variable interest rate.

**Concentrations of Credit Risk**—Financial instruments that potentially subject the Ballet to credit risk consist primarily of cash, cash equivalents, guaranteed investment contracts, accounts and pledges receivable, and investments. The Ballet maintains cash and cash equivalents with major financial institutions. At times, such amounts may exceed Federal Depository Insurance Corporation limits. The Ballet’s investments have been placed with major counterparties. The Ballet closely monitors these investments and its accounts and pledges receivable and has not experienced significant credit losses. As of June 30, 2006, pledges receivable include approximately \$4,740,000 due from members of the Ballet’s Board of Trustees.

**Use of Estimates**—The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

**Comparative Presentation**—The financial statements include certain prior-year summarized comparative information in total, but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the Ballet’s consolidated financial statements for the year ended June 30, 2005, from which the summarized information was derived.

## 2. PLEDGES RECEIVABLE

Pledges receivable at June 30 2006 are due as follows:

<b>Years Ending June 30</b>	
2007	\$4,113,455
2008–2011	3,435,180
Thereafter	<u>43,326</u>
Total pledges receivable	7,591,961
Less allowance for doubtful pledges receivable	(135,531)
Less discount for amounts expected to be collected after one year	<u>(311,527)</u>
Pledges receivable—net	<u>\$7,144,903</u>

## 3. ENDOWMENT INVESTMENTS

The endowment investments consist of the following components, (1) permanently restricted investments which represent the historic dollar value of contributions restricted by donors for permanent investment, (2) temporarily restricted investments from the reinvested net income of endowment investments whose earnings have been restricted by donors for specific purposes, and (3) unrestricted endowment investments which represent funds directed for investment in the endowment by the Ballet's Board of Trustees and the net income from unrestricted endowment investments after expenses associated with raising and managing the endowment funds.

A portion of the accumulated net investment return from the endowment investments is transferred for use in the Ballet's operations each year based on a transfer rate established by the Foundation's Board of Directors (the "Operating Transfer"). For the year ended June 30, 2006, the Operating Transfer was based on a transfer rate of 5% applied to the average of the estimated fair value of the total endowment investments as of March 31, 2003, 2004, and 2005. In addition to the Operating Transfer of approximately \$2,784,000, the Foundation's Board of Directors also approved a supplemental transfer of approximately \$1,526,000 (the "Supplemental Transfer") for the year ended June 30, 2006.

Endowment investments consist of the following at June 30, 2006, at estimated fair value:

Equity investments	\$42,050,236
Fixed income investments	16,514,708
Limited partnership investment	10,223,582
Cash and equivalents held for investment	<u>937,769</u>
Total endowment investments	<u>\$69,726,295</u>

A member of the Foundation's Board of Directors is a General Partner of the limited partnership. A member of the Ballet's Board of Trustees is the Chief Executive Officer of the Foundation's investment custodian.

The following schedule summarizes the investment return from the endowment investments for the year ended June 30, 2006:

Net realized and unrealized gains	\$ 4,495,801
Limited partnership gain	1,193,120
Dividends and interest	<u>1,281,782</u>
Total return on endowment investments	6,970,703
Amount transferred to operations	<u>(4,309,651)</u>
Investment return after transfers to operations	<u>\$ 2,661,052</u>

#### 4. PROPERTY AND EQUIPMENT

The Ballet's property and equipment at June 30, 2006 is as follows:

	Historical Cost	Accumulated Depreciation	Net
Temporarily Restricted:			
Building and improvements	\$ 11,170,688	\$ (5,885,424)	\$ 5,285,264
Furniture and equipment	480,707	(411,149)	69,558
Capitalized sets and costumes	<u>62,745</u>	<u>                    </u>	<u>62,745</u>
Total temporarily restricted	<u>11,714,140</u>	<u>(6,296,573)</u>	<u>5,417,567</u>
Unrestricted:			
Land	571,689		571,689
Building and improvements	14,273,006	(1,339,820)	12,933,186
Furniture and equipment	2,556,654	(1,639,628)	917,026
Capitalized sets and costumes	8,511,346	(5,371,285)	3,140,061
Construction in progress—building	<u>114,414</u>	<u>                    </u>	<u>114,414</u>
Total unrestricted	<u>26,027,109</u>	<u>(8,350,733)</u>	<u>17,676,376</u>
Total property and equipment—net	<u>\$37,741,249</u>	<u>\$ (14,647,306)</u>	<u>\$23,093,943</u>

Depreciation expense was \$1,867,834 for the year ended June 30, 2006.

#### 5. CREDIT FACILITY

The Ballet has a line of credit with a bank of \$1,444,200, secured by certain investment securities in the San Francisco Ballet Endowment portfolio. Interest on the line of credit is charged at the prime rate minus 0.25%. The line of credit expires on January 31, 2007. The Ballet had \$1,368,158 outstanding borrowings under the line of credit as of June 30, 2006. Subsequent to June 30, 2006, the outstanding borrowings were repaid.

## 6. BONDS PAYABLE

On July 3, 2002, the Ballet entered into an agreement with the California Infrastructure and Economic Development Bank for the issuance of \$19,540,000 in Revenue Bonds, Series 2002 (the "Bonds"). The Bonds bore interest at a variable rate (3.95% as of June 30, 2006), matured on various dates from July 1, 2007 through July 1, 2032, and were secured by Gross Revenues of the Ballet, as defined in the Letter of Credit, Reimbursement and Security Agreement with Allied Irish Bank, P.L.C. Interest payments were payable and due on the first of each month. Interest expense for the year ended June 30, 2006 was \$555,525. In connection with the Bonds, the Ballet was required to be in compliance with certain financial covenants.

A schedule of future principal payments required under the Bond indenture at June 30, 2006 is as follows:

<b>Years Ending June 30</b>	
2008	\$ 440,000
2009	500,000
2010	500,000
2011	500,000
Thereafter	<u>17,600,000</u>
Total	<u>\$ 19,540,000</u>

The proceeds from the Bonds were held in restricted cash accounts, and certain conditions were met prior to the release of the funds. The proceeds from the Bonds were used for the renovation and expansion of the Ballet's building; the construction of sets, properties, and costumes for two new full-length ballet productions; the payment of interest and letter of credit fees; and costs incurred in connection with the issuance of the Bonds.

On August 22, 2003, the Ballet entered into a Swap Agreement with respect to the Bonds which effectively fixed the interest rate on a notional amount of \$8,000,000 at 4.44% for the remaining term of the Bonds. The fair value of the Swap Agreement is estimated based on a quote from the market maker of this instrument and represents the estimated amounts the Ballet would expect to receive or pay to terminate the agreement. The estimated fair value of the Swap Agreement was approximately \$(52,000) at June 30, 2006, and is included in interest rate swap liability in the accompanying consolidated statement of financial position. The Swap Agreement also required the Ballet to fund a security deposit in the amount of \$250,000, which was placed in a certificate of deposit with an interest rate of 3.39% maturing on August 19, 2008. The security deposit is included in prepaid expenses and deposits on the accompanying consolidated statement of financial position. Payments made to the counterparty of the Swap Agreement were approximately \$73,000 during the year ended June 30, 2006, and are included in net realized and unrealized (gains) losses on interest rate swap in the consolidated statement of activities and changes in net assets.

Subsequent to year end, the Ballet entered into an agreement to refund the Bonds. In connection with this transaction, the Swap Agreement was also settled (see Note 12).

**7. TEMPORARILY RESTRICTED NET ASSETS AND NET ASSETS RELEASED FROM RESTRICTIONS**

As of June 30, 2006, temporarily restricted net assets were available for the following purposes:

For use in ensuing fiscal years	\$ 4,613,941
Property and equipment	5,488,016
New Ballet production	1,838,731
Ballet school support	933,467
Touring activities	598,000
Education and outreach	345,617
Special events	174,000
Dancers career transition	<u>2,575</u>
Total temporarily restricted net assets	<u>\$13,994,347</u>

Net assets were released from donor restrictions during the year ended June 30, 2006, by incurring expenses satisfying the restricted purposes specified by donors as follows:

Due to the expiration of time	\$3,677,191
Property and equipment	293,976
New Ballet production	150,000
Touring activities	<u>450,000</u>
Total net assets released from restrictions	<u>\$4,571,167</u>

**8. WORKERS' COMPENSATION**

The Ballet's workers' compensation insurance policies include self-insured retention limits and fully insured coverage above such limits. Accruals for claims under the Ballet's self-insured retention limits are recorded on a claim-incurred basis. The estimated liability for workers' compensation claims incurred but unpaid at June 30, 2006, of approximately \$1,318,000 is included in accounts payable and accrued expenses in the accompanying consolidated statement of financial position. At June 30, 2006, the Ballet had unused letters of credit totaling \$2,055,800, as required by the Ballet's insurance carriers.

**9. POSTRETIREMENT AND HEALTH AND WELFARE PLANS**

The Ballet has a defined contribution retirement plan that covers all eligible nonunion employees, and includes a 401(k) component. Contributions approximated \$420,000 for the year ended June 30, 2006, and were made at the discretion of the Ballet.

Substantially, all theatrical employees are covered under collective bargaining agreements that require payments to multiemployer pension, health, and welfare plans. Contributions to these plans approximated \$1,793,900 for the year ended June 30, 2006.

## 10. LEASE COMMITMENTS

The Ballet rents performance space, student residence facility, and storage space under various operating leases. The following is a schedule of future minimum rental payments required under operating leases that have initial noncancelable lease terms in excess of one year:

<b>Years Ending June 30</b>	
2007	\$ 326,000
2008	195,000
2009	37,000
2010	38,000
2011	<u>33,000</u>
Total	<u>\$ 629,000</u>

Rent expense from operating leases approximated \$530,000 for the year ended June 30, 2006.

## 11. CONTINGENCIES

The Ballet is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Ballet's financial position or its changes in net assets.

## 12. SUBSEQUENT EVENTS

On August 2, 2006, the Ballet entered into an agreement with the California Infrastructure and Economic Development Bank for the issuance of \$44,000,000 in Variable Rate Revenue Bonds, Series 2006 (the "New Bonds") and refunded the \$19,540,000 in Revenue Bonds, Series 2002 described in Note 6. The New Bonds bear interest at a variable rate (3.25% at August 2, 2006), mature on various dates from July 1, 2027 through July 1, 2036, and are an unsecured obligation of the Ballet and the Foundation, and are insured by the FGIC Insurance Company. The proceeds from the New Bonds are held in restricted cash accounts, and certain conditions must be met prior to the release of the funds. In addition to the refund of the Revenue Bonds, Series 2002, the proceeds from the New Bonds will be used for the purchase and renovation of a warehouse, student residence, and construction of ballet sets and costumes. As part of the issue of the New Bonds, the Ballet entered into a Swap Agreement which effectively fixed the interest rate on a notional amount of \$22,000,000 at 3.922% for the remaining term of the New Bonds. At the same time, the Swap Agreement outstanding at June 30, 2006 was settled.

As a result of the above transaction, the 2007 statement of activities and changes in net assets will reflect the write-off of the remaining bond issuance costs related to the Revenue bonds, Series 2002 of \$382,440 at June 30, 2006, the settlement of the Swap Agreement outstanding at June 30, 2006 for a cost of \$129,000 and the noncash impact of the refunding of the Revenue Bonds, Series 2002.

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